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No. 426

In the Supreme Court of the United States

OCTOBER TERM, 1939

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, PETITIONER

v.

STEPHEN J. LEONARD

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR THE PETITIONER

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OPINIONS BELOW

The opinion of the Board of Tax Appeals (R. 11–21) is reported in 36 B. T. A. 563. The opinion of the Circuit Court of Appeals (R. 76–80) is reported in 105 F. (2d) 900.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered on July 20, 1939 (R. 80.) The petition for a writ of certiorari was filed September 29, 1939, and was granted February 5, 1940. The

jurisdiction of this Court rests on Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether payments to respondent's divorced wife from the income of a trust which was created by him for her maintenance and support and which was ratified in the divorce decree of a New York court should be included in his taxable income.

STATUTES AND REGULATIONS INVOLVED

The statutes and regulations involved are set forth in the Appendix, *infra*, pp. 25–28.

STATEMENT

The material facts, as found by the Board of Tax Appeals (R. 12–16), are as follows:

On December 27, 1928, the wife of the taxpayer, who was then living apart from him, began suit for divorce against him in New York. (R. 12.) While this action was pending, the taxpayer and his wife executed a deed of trust and a separation agreement, both on June 4, 1929. (R. 12, 14.)

The deed conveyed securities and cash valued at $650,000 [1] from the taxpayer to a trustee in trust to pay the net income to the beneficiaries therein

[1] Included in that amount were bonds of an aggregate face amount of $400,000 which petitioner himself guaranteed as to principal and interest, and in case of default he agreed to substitute cash or securities in lieu thereof. (R. 13.)

named in equal monthly installments so far as practicable. (R. 12–13.) During the life of the wife, the trustee was to pay from the net income $5,000 per year to each of three named children or to the wife as guardian during their minority. The remaining net income was payable to the wife for her support and maintenance. (R. 13.) Upon the death of the wife, the trust fund was to be divided into as many parts as there were children of the grantor by the wife, each part to constitute a separate trust fund for the benefit of each child as life beneficiary. Upon the death of each life beneficiary, the corpus was to be paid as directed by the will of such beneficiary. (R. 13–14.)

The separation agreement incorporated by reference the deed of trust and recited the expectation of both parties that the wife would receive $30,000 per year from the aggregate net income from the trust and from property given to her by the taxpayer in the past. (R. 14–15.) The taxpayer promised to make additional payments of $35,000 per year to his wife for life, provided his circumstances and ability to pay continued as good as of that date, so as to bring the total allowance for her support and maintenance to $65,000 per year. (R. 15.) The wife accepted the establishment of the trust fund and the payments to be made pursuant to the separation agreement in lieu of all dower and released any claim of dower in the property of the taxpayer. (R. 15.)

The divorce decree became final October 22, 1929.

The court incorporated the agreements in the decree, "approved and affirmed" the same, and directed the taxpayer to pay his wife $35,000 per annum during her life. (R. 16.)

Between June 4 and December 31, 1929, the trustee received income of $16,191.34 from the trust property. It distributed $5,200 to the wife and five-twelfths of $5,000, or $2,083.33, to each of the three children, leaving an undistributed balance for that period of about $4,700. (R. 16.) The Commissioner included all of this income in the taxpayer's taxable income for 1929. (R. 16, 11–12.) Upon review, the Board of Tax Appeals held that only the amounts actually distributed to taxpayer's wife and minor children were taxable to him and that the portions paid to his adult daughter and undistributed were not so taxable. Both the Commissioner and the taxpayer appealed, and the court below, reversing the decision of the Board, held that although the taxpayer was taxable on income payable to his minor children, he was not taxable on income payable to the wife.

SPECIFICATION OF ERRORS TO BE URGED

The Circuit Court of Appeals erred:

1. In holding that the taxpayer was not taxable upon trust income payable to his wife for her support and maintenance under the terms of the trust agreement here involved.

2. In failing to hold the taxpayer taxable under *Douglas* v. *Willcuts*, 296 U. S. 1.

3. In holding that *Douglas* v. *Willcuts* is inapplicable unless by state law the divorce court retains power to change its original alimony award.

4. In not holding that under New York law the terms of the instant divorce decree regarding support of the wife may be changed or modified as justice may require.

5. In failing to affirm and in reversing the decision of the Board of Tax Appeals in so far as it held that the taxpayer is taxable on trust income paid to his wife.

6. In affirming and in not reversing the decision of the Board of Tax Appeals in so far as it held the taxpayer not taxable on trust income received in 1929 and currently distributable to the wife but not actually distributed during the taxable year.

SUMMARY OF ARGUMENT

The trust was created for the purpose of discharging taxpayer's subsisting obligation to support his wife. It was ratified by the divorce court as a means by which he was to discharge that duty after the divorce. The income from the trust is therefore taxable to the taxpayer, just as though he had received it and then paid it over to his wife. *Douglas* v. *Willcuts*, 296 U. S. 1.

That the divorced wife must look solely to the trust is immaterial. It was the act of the taxpayer which permanently devoted the trust income to his obligation. The trust itself is in substance equivalent to a continuing exercise by the settlor

of the power to direct the application of the income along the predetermined channels.

There is no essential difference between the case at bar and *Douglas* v. *Willcuts*. Although the Minnesota court in *Douglas* v. *Willcuts* had the power to modify the alimony decree thereafter, the fact that such continuing power of modification may be absent in New York is inconsequential. In any event, however, the New York law does permit the divorce court to alter the alimony decree, so that even this alleged difference between *Douglas* v. *Willcuts* and the instant case vanishes.

ARGUMENT

THE TRUST INCOME IS TAXABLE TO THE HUSBAND UNDER THE DOCTRINE OF *DOUGLAS* v. *WILLCUTS*

Introductory.—Taxpayer and his wife executed a deed of trust and a separation agreement on June 4, 1929, when the wife's suit for a divorce was pending. The trust deed provided for certain payments to their children, with the remaining net income payable to the wife for her support and maintenance. (R. 13–14.) The divorce decree, which became final October 22, 1929, incorporated the agreements and "approved and affirmed" them. (R. 16.)

The court below held that the amounts payable to the wife from the trust were not includible in taxpayer's income. In reaching that result, the Circuit Court of Appeals interpreted the doctrine of *Douglas* v. *Willcuts*, 296 U. S. 1, as embracing only those "alimony trust" situations in which the

divorce court, by the terms of its decree or the applicable state law, retains the power to change its original award. Having so construed *Douglas* v. *Willcuts,* the court ruled that under the law of New York the divorce court retained no continuing power to modify the provisions for the wife, and accordingly gave judgment in favor of the taxpayer.

In *Helvering* v. *Fitch,* decided January 29, 1940, No. 243, this Court held that the income from the "alimony trust" there involved was taxable to the husband under the general rule enunciated in *Douglas* v. *Willcuts.* In the presentation of the *Fitch* case, the Government argued, first, that the existence of a continuing power in the divorce court to modify the provision for the wife is not a necessary condition to the applicability of *Douglas* v. *Willcuts,* and that, in any event, under applicable Iowa law the divorce court retained the power to modify. This Court held in favor of the Government on the ground that the taxpayer had failed to show by clear and convincing proof that the Iowa court had no continuing jurisdiction, without passing upon the Government's contention that *Douglas* v. *Willcuts* should apply regardless of the local law as to power of the divorce court to change its original award.

1. Assuming, *arguendo,* that the court below was correct in holding that under the law of New York the divorce court retained no continuing power, we again respectfully submit that *Douglas* v. *Willcuts*

should nevertheless control, that there is a functional identity between the two trusts which should not be subject to diverse tax consequences.

In *Douglas* v. *Willcuts*, a husband, in anticipation of divorce, had created a trust for his wife to pay her $15,000 a year for a fixed period, and $21,000 a year thereafter. Excess income was to be paid to him, but in the event of any deficiency in income the trustee could call upon him for the difference, and upon his failure to pay the difference the trustee was authorized to make up the deficiency out of corpus. The parties had agreed that these provisions for the wife were "in lieu of, and in full settlement of alimony, and of any and all dower rights or statutory interests in the estate" of her husband, and "in lieu of any and all claims for separate maintenance and allowance for her support" (p. 3). A divorce decree entered thereafter provided that the provisions in the trust for the wife's benefit were to be in lieu of all alimony or interest in the property of the husband. In holding the husband taxable with respect to the income of that trust, this Court said (pp. 8–9):

> Amounts paid to a divorced wife under a decree for alimony are not regarded as income of the wife but as paid in discharge of the general obligation to support, which is made specific by the decree. * * * Petitioner's contention that the district court did not award alimony is not supported by the terms of the decree. It described the provision as made "in lieu of all *other*

alimony or interest in the property or estate of the defendant." However designated, it was a provision for annual payments to serve the purpose of alimony, that is, to assure to the wife suitable support. The fact that the provision was to be in lieu of any other interest in the husband's property did not affect the essential quality of these payments. Upon the preexisting duty of the husband the decree placed a particular and adequate sanction, and imposed upon petitioner the obligation to devote the income in question, through the medium of the trust, to the use of his divorced wife.

* * * We have held that income was received by a taxpayer, when, pursuant to a contract, a debt or other obligation was discharged by another for his benefit. * * * The creation of a trust by the taxpayer as a channel for the application of the income to the discharge of his obligation leaves the nature of the transaction unaltered. *Burnet* v. *Wells, supra.* In the present case, the net income of the trust fund, which was paid to the wife under the decree, stands substantially on the same footing as though he had received the income personally and had been required by the decree to make the payment directly.

These principles have been applied in a large number of cases: *Helvering* v. *Coxey,* 297 U. S. 694, reversing *per curiam* 79 F. (2d) 661 (C. C. A. 3d); *Helvering* v. *Schweitzer,* 296 U. S. 551, reversing *per curiam* 75 F. (2d) 702 (C. C. A. 7th), rehearing

denied, 296 U. S. 665; *Helvering* v. *Stokes*, 296 U. S. 551, reversing *per curiam* 79 F. (2d) 256 (C. C. A. 3d), rehearing denied, 296 U. S. 665; *Helvering* v. *Blumenthal*, 296 U. S. 552, reversing *per curiam* 76 F. (2d) 507 (C. C. A. 2d); *Donnelley* v. *Commissioner*, 101 F. (2d) 879 (C. C. A. 7th), certiorari denied, 307 U. S. 645; *Glendinning* v. *Commissioner*, 97 F. (2d) 51 (C. C. A. 3d); *Alsop* v. *Commissioner*, 92 F (2d) 148 (C. C. A. 3d), certiorari denied, 302 U. S. 767, rehearing denied, 303 U. S. 666; *Hill* v. *Commissioner*, 88 F. (2d) 941 (C. C. A. 8th); *Commissioner* v. *Grosvenor*, 85 F. (2d) 2 (C. C. A. 2d).

The law of New York imposed upon the taxpayer the obligation to support his divorced wife. New York Civil Practice Act, Ann., Book 6, Sections 1170, 1155, Appendix, *infra*, pp. 26–27. The decree of the divorce court incorporated, "approved and affirmed" the separation agreement, which in turn incorporated the trust. To paraphrase *Douglas* v. *Willcuts*, the decree of the divorce court placed a particular and adequate sanction upon the husband's preexisting duty and required him to discharge his obligation by devoting the income in question, through the medium of the trust, to the use of his divorced wife. That income stands substantially on the same footing as though he had received it personally and discharged his obligation by paying it over to his wife. Here, as in *Douglas* v. *Willcuts*, the trust income serves as a substitute for payments made directly by the hus-

band, and confers on him in every real sense a direct benefit which constitutes taxable income.

The court below, however, undertook to distinguish *Douglas* v. *Willcuts* on the ground that under Minnesota law the divorce court was empowered, at any time after the divorce, to modify the alimony decree, whereas under New York law, no such power was thought to exist. Hence, the court reasoned, there was no continuing obligation on the husband to the satisfaction of which the trust income was devoted. But it is manifestly not essential to the existence of a continuing obligation that the amount thereof be subject to *increase*. If there is a continuing obligation, income devoted to its satisfaction is taxable to the obligor whether the amount of the obligation be subject to modification or be inalterably fixed.[2]

In the instant case, even though there was no recourse against the husband beyond the terms of the trust, he was nevertheless subject to a continuing obligation to support his divorced wife. Under the law of New York, the husband's obligation of support did not terminate upon the granting of an

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[2] Thus, it is clear that if A is legally obligated to pay B $5,000 and no more annually during B's life, and the payments to B are made by C, A realizes income in the amount of the payments by C to B for his benefit. Cf. *Old Colony Tr. Co.* v. *Commissioner*, 279 U. S. 716; *United States* v. *Boston & M. R. Co.*, 279 U. S. 732. The result is the same where taxpayer creates a trust the income of which is applied to the discharge of his obligation. *Helvering* v. *Blumenthal*, 296 U. S. 552. Cf. *Burnet* v. *Wells*, 289 U. S. 670.

absolute divorce. *Daggett* v. *Daggett,* 5 Paige (N. Y.) 509; *Hamlin* v. *Hamlin,* 230 N. Y. S. 51. On the contrary, the New York statute expressly provided that in an action for divorce brought by the wife "the court * * * must give, either in the final judgment, or by one or more orders, made from time to time before final judgment, such directions as justice requires * * * for the support of the plaintiff". New York Civil Practice Act, Book 6, Section 1170. See also Section 1155, Appendix, *infra.* In decreeing alimony, the divorce court merely makes specific the husband's general and continuing obligation to support the wife. *Audubon* v. *Shufeldt,* 181 U. S. 575, 577; *Romaine* v. *Chauncey,* 129 N. Y. 566, 570. If the court, in its final order, had simply ordered the payment to the wife of a designated annual income, the husband's obligation would assuredly have been a continuing one, regardless of the assumed inability of the court to change such order.

The situation is no different because the court adopted the agreement of the parties. An agreement as to the support of the wife will be upheld by the divorce court only if its provisions are fair and equitable, for the husband's continuing obligation to support the wife as long as she lives can not be avoided by an unconscionable contract. *Daggett* v. *Daggett, supra; Hamlin* v. *Hamlin, supra.* Thus, in adopting the agreement, the New York court simply ruled in substance that the just provision for the wife, which it was required by

statute to order, coincided with what the parties had themselves arranged. Accordingly, the court ordered the husband to do as he had agreed. But the fact that the court, in delineating the extent of the husband's future liability, determined it as coextensive with what the parties had agreed did not terminate the husband's obligation. The court's acceptance of the parties' agreement merely indicated that the court believed its provisions were "as justice requires". Had the court deemed the agreement unjust, it could have imposed on the husband an additional or different continuing obligation.

The decree of the court recognized the husband's preexisting duty to support, and defined that duty as coextensive with what the parties had themselves arranged. Thus, the trust income served to satisfy and discharge the husband's continuing obligation under the law of New York, as defined in the final order by the court. We submit that such income is therefore taxable to the husband. The fact that in the *Douglas* case the Minnesota court could later modify its final decree provided a striking illustration of the fact that the trust income was there devoted to the discharge of taxpayer's continuing obligation, but that circumstance was not essential to the decision. *The critical element is that the duty to support after divorce existed at the time the trust was executed, and the grantor simply carved out future income*

from property which he then owned and devoted it in advance to the discharge of that obligation.

The Court in *Douglas* v. *Willcuts* likewise commented at some length (296 U. S. 1, 8) upon the fact that the Minnesota court—

> did not approve the trust agreement as one deriving efficacy from the action of the parties. The court made its own requirement. The decree required the petitioner to "provide and create the trust fund." While the terms of the trust as set up in the trust agreement were approved, the court made those terms its own. It was from this action of the court that the trust derived its force.

Yet, within three months, in *Helvering* v. *Coxey*, 297 U. S. 694, the Court ruled *per curiam* that the grantor of an alimony trust was taxable, even though the decree of the state court made no mention whatever of the trust. We believe that the continuing power of the Minnesota court, together with the grantor's contingent liability to make up deficiencies, were no more essential to the decision in *Douglas* v. *Willcuts* than was the fact that the Minnesota court ratified and adopted the trust.

The important consideration in *Douglas* v. *Willcuts* was, we submit, that the trust operated to discharge the taxpayer's obligation to his wife, whether or not that obligation could be increased, or whether or not it was fortified by a contingent liability to make up deficiencies. In New York, as in Minnesota, the divorce court may mark out the husband's duty of future maintenance, and

enter an appropriate order. And where the court determines that the income from a trust established by the husband is adequate provision for such maintenance, the subsequent application of that income carries out that obligation, and should be taxable to the husband.

This case differs from *Douglas* v. *Willcuts* only as to the *extent* of the obligation, rather than its *continued existence.* In both situations the husband had, at the time of the divorce decree, an obligation toward his wife. In both cases, the divorce court marked out the limits of that obligation. In *Douglas* v. *Willcuts,* that obligation was subject to possible increase by the divorce court, whereas we are assuming that the divorce court in the present case lacked such power. But in each case, the income was applied to the discharge of the obligation recognized by the divorce court. And in both, the trusts were merely the predetermined channels for the application of the income to the discharge of the husband's duty to support. The absence of power in the divorce court to decree an expansion of the extent of that duty does not change the essential quality of the trust income as applied in lieu of alimony.

With regard to the extent of the obligation, as distinguished from its *continuance,* the instant case differs further from *Douglas* v. *Willcuts* in that the husband here did not undertake to make good deficiencies in the income of the trust. However, we contend that *Douglas* v. *Willcuts* is applicable

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irrespective of a guaranty by the husband against deficiency in trust income. It is true that, in stating the facts in the *Douglas* case, this Court briefly mentioned that "Deficiencies were to be made up in a prescribed manner" (296 U. S. 3), but that fact was not even adverted to in the remainder of the opinion and we submit it was not necessary to the result.

If the applicability of *Douglas* v. *Willcuts* is made dependent upon an undertaking to make up deficiencies in trust income, the emasculation of the vital principle of the case would assuredly result. Tax liability could readily be avoided while substantially guaranteeing the wife's income from the trust by a variety of artful provisions in the trust instrument. The husband, while refraining from an express guaranty that the wife would receive a designated sum annually, could guarantee the principal and interest on bonds constituting the entire trust corpus. This was almost the situation in the instant case, where the husband guaranteed bonds, both as to principal and interest, of a value of $400,000 out of a total trust corpus of $650,000. (R. 12–13.) Or, in conjunction with the establishment of a trust, the husband might agree personally to pay the wife in addition a specified sum, say $20,000 per year, subject to modification from time to time by the divorce court, depending on circumstances. Any decrease in the trust income would undoubtedly be a factor to be considered by the

court in determining the amount of the additional payments from the husband.[3] Similarly, a husband desirous of providing an annual income for the divorced wife of $5,000 might create a trust of such size that its normal income would be $10,000 and provide that from the trust income $5,000 was first to be paid to the wife, and the balance to him, thereby affording the wife a comfortable margin of security that her alimony would be paid.[4] Likewise, the trust instrument might provide that if the trust income fell below the amount payable to the divorced wife, the husband would assign certain

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[3] The instant case does in fact involve a similar feature. By the terms of the separation agreement approved and incorporated in the final decree, the husband was to pay the wife $35,000 per year, subject to reduction to not less than $10,000 by the divorce court. (R. 36.) Although the agreement makes the husband's circumstances and ability to pay the test for granting any reduction, as pointed out by the court below (R. 78), the divorce court might take into account the wife's other means, in which case any diminution in income from the trust would be a factor in determining the amount of the payments from the husband. Should the amount payable annually be once reduced from the maximum of $35,000 permitted by the agreement any subsequent decrease in trust income might be reflected in an increase in the husband's personal liability.

[4] Such a situation obtained in *Helvering* v. *Fitch*, *supra*, decided January 29, 1940, where the trust income was $12,000 per year, of which only $7,200 was payable to the wife, with the remainder going to the husband. Yet one of the reasons for which the Circuit Court of Appeals for the Eighth Circuit held that *Douglas* v. *Willcuts* was inapplicable was the absence of an undertaking to make up deficiencies. 103 F. (2d) 702.

designated securities to the trust to make up the deficiency.[5]

By adroit utilization of any of the foregoing, or similar, arrangements, or a combination of two or more of them, the husband in nearly every case could substantially insure his wife a specified annual income without personally assuming responsibility to make up any deficiencies. As a practical matter, the difference between such a situation and *Douglas* v. *Willcuts* would be negligible. Yet if liability to make up a hypothetical deficiency is regarded as essential, the husband in such a situation would not be subject to tax. We believe that this Court could not have intended *Douglas* v. *Willcuts* to be thus drastically limited by so attenuated and meaningless a distinction.

Moreover, the result reached below permits the husband to circumvent an express prohibition in the statute and regulations. Section 24 (a) (1), of the Revenue Act of 1928, Appendix, *infra,* provides that no deduction shall be allowed in respect of "Personal, living, or family expenses", and Article 281 of Regulations 74, *infra,* construing the statute, provides that alimony may not be deducted from gross income. Had the grantor held the property without the interposition of the trust, and

[5] This was the situation in *Dixon* v. *Commissioner* (C. C. A. 3d), decided January 10, 1940, not yet officially reported but found in 1940 C. C. H., Vol. 4, p. 9462, in which it was held that *Douglas* v. *Willcuts* was inapplicable because there was no personal guaranty by the husband of the wife's income.

simply paid out the income therefrom to his wife as alimony he would have been chargeable with the full amount of that income and would not have been entitled to any deduction on account of the alimony paid out. The decision below permits him to achieve the same result by creating a trust, but without rendering him liable for tax with respect to the income. In essence, it awards him the very deduction that Congress has denied him.

Furthermore, the basic issue before the Court is whether the income in question falls within the definition of gross income as set forth in Section 22 (a), *infra*, and the broad sweep of that definition has often been said to be coextensive with the power of Congress under the Constitution. *Helvering* v. *Stockholms &c. Bank*, 293 U. S. 84, 89; *Douglas* v. *Willcuts*, *supra*, at p. 9; *United States* v. *Safety Car Heating Co.*, 297 U. S. 88, 93; *Helvering* v. *Midland Ins. Co.*, 300 U. S. 216, 223; *Irwin* v. *Gavit*, 268 U. S. 161, 166; *Helvering* v. *Clifford*, No. 383, present Term, decided February 26, 1940. However, it seems clear beyond question that there can be no constitutional objection to the tax here involved. For, in *Burnet* v. *Wells*, 289 U. S. 670, this Court sustained a tax upon the grantor of an irrevocable trust established to pay premiums on policies of insurance taken out on his own life for the benefit of others. No legal obligation of any kind was there involved. At most the trust served to discharge a moral obligation owed by the grantor to his family. Yet it accomplished a result which

to him was desirable, and which he would otherwise have been compelled to achieve by the use of his own funds or unrestricted income. By employing an irrevocable trust, he had merely devoted a portion of his future income to that end. The Court commented upon the various trust devices employed in order to defeat taxes in which the common element was the surrender of title to another while retaining the substance of enjoyment. And in sustaining the tax, the Court remarked (p. 677):

> At times escape has been blocked by the resources of the judicial process without the aid of legislation. * * * In these and other cases there has been a progressive endeavor by the Congress and the courts to bring about a correspondence between the legal concept of ownership and the economic realities of enjoyment or fruition. * * *

2. Thus far, we have urged that *Douglas* v. *Willcuts* applies without regard to the continued power of the divorce court to modify the decree or the existence of a contingent obligation to make up any hypothetical deficiencies in trust income. And for the purpose of argument we assumed that the court below had correctly interpreted the New York law as forbidding any subsequent modifications of the alimony decree. However, we believe that the court erred in its interpretation of the New York law, and that the power to modify does exist in New York.

Sections 1155 and 1170 of the New York Civil Practice Act, Appendix, *infra*, specifically and un-

equivocally confer on the divorce court the power to "annul, vary or modify" its direction for the support of the wife "at any time after final judgment". Moreover, Section 51 of the New York Domestic Relations Law, Appendix, *infra,* forbids a wife from making an agreement discharging her husband's duty to support her. The court below referred to these statutory provisions (R. 78), but held that nevertheless, under the New York decisions, a settlement is finally binding upon the parties in the absence of fraud, duress, etc.

In so holding, the court relied upon *Galusha* v. *Galusha,* 116 N. Y. 635. But that case was decided prior to the enactment of Section 21 of the Domestic Relations Law of 1896 (New York Laws, 1896, Vol. 1, c. 272, p. 220) from which was derived Section 51, applicable here. Moreover, that case appears to be inconsistent with *Daggett* v. *Daggett,* 5 Paige (N. Y.) 509, not there overruled, which was cited with approval and followed, after the *Galusha* decision, in *Dailey* v. *Dailey,* 9 Misc. (N. Y.) 511, 514. The only other authorities upon which the court below based its conclusion as to the New York law are *Cain* v. *Cain,* 188 App. Div. (N. Y.) 780, and *Hamlin* v. *Hamlin,* 224 App. Div. (N. Y.) 168, both decided by the Fourth Department of the Appellate Division of the New York Supreme Court. Although the *Cain* case does appear to afford some support for the court's view of the New York law, the later *Hamlin* case held that an agreement providing for the support of the

wife could be modified by the divorce court where its terms were inadequate and unfair.

Under the New York statute, although the final judgment of divorce ends the relationship of husband and wife, the husband's obligation of support is continued in the form of alimony, and the court's jurisdiction over the parties and the incidental subject matter does not terminate. *Fox* v. *Fox*, 263 N. Y. 68, 70; *Winter* v. *Winter*, 191 N. Y. 462, 473–474. Moreover, an agreement providing for the wife will be set aside if unfair and unequitable. *Hamlin* v. *Hamlin*, 224 App. Div. (N. Y.) 168; cf. *Tirrell* v. *Tirrell*, 232 N. Y. 224; *Hungerford* v. *Hungerford*, 161 N. Y. 550.

In *Kunker* v. *Kunker*, 230 App. Div. (N. Y.) 641, the Appellate Division of the Supreme Court, Third Department, expressly held that the court has power to modify its judgment, in an action for absolute divorce, and change the provision for support, notwithstanding an agreement for support was incorporated and approved in the final decree. The court declared that upon the incorporation of the agreement in the judgment, it became a part thereof, and that the statutory power to modify the judgment is not divested merely because it was based on a formal agreement rather than a stipulation or evidence. This case is squarely in point, and sustains our contention that the divorce court in the present case retained the power to modify the provision for the wife. The court below dismissed *Kunker* v. *Kunker* as a mere aberration, at

variance with New York decisions. The fact remains, however, that the *Kunker* case has been consistently followed by the New York courts,[6] has been approved or followed in all four departments of the Appellate Division of the New York Supreme Court,[7] and is consistent with the decisions of the Court of Appeals.

We believe that the clear language of the New York statutes (Sections 1155 and 1170) of the Civil Practice Act, and Section 51 of the Domestic Relations Law), together with the foregoing decisions, particularly *Kunker* v. *Kunker,* established clearly that the New York law empowered the divorce court to modify the provisions for the wife contained in its final decree. But in any event, under the decision of this Court in the *Fitch* case, the burden is on the taxpayer to show, "by clear and convincing proof" that under the New York law the divorce court retains no power to modify. At most, that conclusion could be based on no more than "mere

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[6] See, for example, *Schnitzer* v. *Buerger*, 237 App. Div. 622, 624 (1st Dept.), and *Staehr* v. *Staehr*, 237 App. Div. 843 (2d Dept.).

See also *Goldstein* v. *Goldsmith*, 243 App. Div. 268, 271 (2d Dept.); *Dworkin* v. *Dworkin*, 247 App. Div. 213, 214 (1st Dept.); *Holahan* v. *Holahan*, 234 App. Div. 572, 574 (4th Dept.); *Severance* v. *Severance*, 235 App. Div. 799 (2d Dept.); *Mandel* v. *Mandel*, 235 App. Div. 821 (2d Dept.).

[7] Although *Kunker* v. *Kunker* may be out of harmony with one of the decisions of the Fourth Department cited by the court below (R. 78), namely, *Cain* v. *Cain*, 188 App. Div. 780, it is probably consistent with the other and later one, *Hamlin* v. *Hamlin*, 224 App. Div. 168, 172.

inferences and vague conjectures", in the face of plainly contrary statutory language. Accordingly, under the rule announced in *Helvering* v. *Fitch*, the instant case is governed by *Douglas* v. *Willcuts*.

CONCLUSION

The decision of the court below should be reversed.

Respectfully submitted.

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APPENDIX

Revenue Act of 1928, c. 852, 45 Stat. 791:

SEC. 22. GROSS INCOME.

(a) *General definition.*—"Gross income" includes gains, profits, and income derived from salaries, wages, or compensation for personal service, of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever.

* * * * *

SEC. 24. ITEMS NOT DEDUCTIBLE.

(a) *General rule.*—In computing net income no deduction shall in any case be allowed in respect of—

(1) Personal, living, or family expenses;

* * * * *

Treasury Regulations 74, promulgated under the Revenue Act of 1928:

ART. 83. *Gifts and bequests.*—Property received as a gift, or received under a will or under statutes of descent and distribution, is exempt from the income tax, although the income therefrom derived from investment, sale, or otherwise is not. An amount of principal paid under a marriage settlement is a gift. Neither alimony nor an allowance

based on a separation agreement is taxable income. (See article 281.)

ART. 281. *Personal and family expenses.*—* * * Alimony and an allowance paid under a separation agreement are not deductible from gross income. (See article 83.) * * *

New York Civil Practice Act, Book 6:

§ 1155. *Maintenance and support of wife and children in action for divorce by wife*

The court, in the final judgment dissolving the marriage in an action for divorce brought by the wife, may require the defendant to provide suitably for the education and maintenance of the children of the marriage, and for the support of the plaintiff, as justice requires, having regard to the circumstances of the respective parties; and, by order, upon the application of either party to the action, and after due notice to the other, to be given in such manner as the court shall prescribe, at any time after final judgment whether heretofore or hereafter rendered, may annul, vary or modify such a direction. But no such application shall be made by a defendant unless leave to make the same shall have been previously granted by the court by order made upon or without notice as the court in its discretion may deem proper after presentation to the court of satisfactory proof that justice requires that such an application should be entertained.

§ 1170. *Custody and maintenance of children, and support of plaintiff in action for divorce or separation*

Where an action for divorce or separation is brought by either husband or wife, the

court, except as otherwise expressly prescribed by statute, must give, either in the final judgment, or by one or more orders, made from time to time before final judgment, such directions as justice requires, between the parties, for the custody, care, education, and maintenance of any of the children of the marriage, and where the action is brought by the wife, for the support of the plaintiff. The court, by order, upon the application of either party to the action, or any other person or party having the care, custody and control of said child or children pursuant to said final judgment or order, after due notice to the other, to be given in such manner as the court shall prescribe, at any time after final judgment, may annul, vary or modify such directions, or in case no such direction or directions shall have been made, amend it by inserting such direction or directions as justice requires for the custody, care, education and maintenance of any such child or children or for the support of the plaintiff in such final judgment or order or orders. But no such application shall be made by a defendant, or any other person or party having the care, custody and control of said infant or infants, unless leave to make the same shall have been previously granted by the court by order made upon or without notice as the court in its discretion may deem proper after presentation to the court of satisfactory proof that justice requires that such an application should be entertained. (Amended by L. 1921, ch. 199; L. 1925, ch. 240, in effect Sept. 1, 1925.)

The last sentence of Section 1170 was omitted by Laws of 1934, c. 521, in effect September 1.

New York Domestic Relations Law (McKinney's Consolidated Laws of New York, Book 14):

> § 51. *Powers of married woman.*—A married woman has all the rights in respect to property, real or personal, and the acquisition, use, enjoyment and disposition thereof, and to make contracts in respect thereto with any person, including her husband, and to carry on any business, trade or occupation, and to exercise all powers and enjoy all rights in respect thereto and in respect to her contracts, and be liable on such contracts, as if she were unmarried; but a husband and wife can not contract to alter or dissolve the marriage or to relieve the husband from his liability to support his wife. * * *

The foregoing provisions of the Civil Practice Act and the Domestic Relations Law were in force in 1929 when the trust and separation agreements in this case were executed and the divorce granted; and, except as above indicated, those provisions have not subsequently been altered or amended.

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